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RUEHPE/AMEMBASSY LIMA PRIORITY 1430  
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TREASURY FOR S. GOOCH  
DEPT FOR WHA/EPSC FAITH CORNEILLE

E.O. 12958: N/A  
TAGS: [EINV](#) [ENRG](#) [ECON](#) [EC](#)

SUBJECT: NEW LEGAL ADVISOR A PRACTICAL ADDITION TO ENERGY MINISTRY

REF: A. 06 QUITO 1735

[1](#)B. 06 QUITO 2465  
[1](#)C. QUITO 321

[1](#)1. (SBU) Summary: In a meeting between EconCouns and new Ministry of Energy Legal Advisor Raul Moscoso February 22, Moscoso confirmed that the GOE is assembling a legal team to defend its interests in the Oxy arbitration, and stressed the administration's interest in foreign investment in the energy sector and in solving investment disputes with U.S. companies. He also noted possible changes in the mining sector. End Summary.

#### Ecuador to Participate in Oxy Arbitration

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[1](#)2. (SBU) Moscoso confirmed reports from the press and from other sources that the GOE is assembling a legal team to defend its interests in the international arbitration case under the ICSID brought by Occidental Petroleum (Oxy). While the Correa administration has previously made statements to the effect that the arbitration is invalid, it appears they will now participate in the process to defend Ecuador's actions. Moscoso emphasized that the GOE needs to respect agreements such as the Bilateral Investment Treaty (BIT) with the United States.

[1](#)3. (SBU) The GOE has created a commission to define its strategy for the arbitration, consisting of legal representatives from the Procurador's office, the Foreign Ministry, state oil company Petroecuador, the Energy Ministry (to be represented by Moscoso), and the operator of Oxy's former fields. Moscoso confirmed that the GOE has contracted a "prestigious" U.S. law firm for the arbitration. From an outside source, post has learned that the U.S. lawyer would be Paul Reichler (of DC law firm Foley Hoag); in December the then-Procurador General (Solicitor General) told the Embassy that he intended to hire Reichler to represent the GOE in the Oxy case. Moscoso also confirmed that the GOE's initial defense will be that ICSID does not have jurisdiction to hear the case. Oxy reports that the ICSID tribunal held an initial meeting the week of February 12 to organize, and will likely start formal hearings the first week in May.

#### Administration Favors Investment; Seeks Solutions

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[1](#)4. (SBU) Moscoso stressed that the administration wants to promote investment in the energy sector, and mentioned that efforts to solve GOE disputes with U.S. firms Machala Power and City Oriente are "in process."

15. (SBU) U.S. electricity company Machala Power has brought an international arbitration case against the GOE for underpayment (see Ref A for a discussion of electricity sector underpayment problems in Ecuador), but is attempting to work out a resolution with the GOE outside of the arbitral process. Machala Power had planned a second and third phase of investment that would provide 180 additional megawatts of low cost electricity to Ecuador, but the investment is currently on hold pending resolution of the payment dispute. Moscoso stressed the importance of Machala continuing with its investment and noted the faster the dispute can be resolved, the better. However, Moscoso also noted that the GOE does not currently have the funds to pay Machala and suggested they might offer payment in government bonds instead. (Note: The prior government had also suggested payment in bonds. At that time, Machala Power representatives told the Embassy the company's interest in the proposal would depend largely on whether it could resell the bonds and whether it received a premium for accepting the bonds in lieu of cash.)

16. (SBU) EconCouns asked if the GOE would also develop a plan to ensure that Machala Power would be fully paid in the future. Moscoso did not provide a clear response, and instead characterized the meetings with Machala as being in a "climate of transaction" and stressed that the GOE wants to come to an agreement with Machala and end the arbitration proceedings. Machala Power reports the first ICSID hearing on jurisdiction will be held Monday February 26, and they will meet again with the GOE following the hearing.

17. (SBU) Regarding the dispute with petroleum company City Oriente (Ref B), Moscoso noted that since City is a small firm, the GOE might negotiate a change to City's contract that would exempt them from the hydrocarbons reform law. Noting that the revisions to the hydrocarbons law apply to large, production-sharing contracts, Moscoso suggested that City might be able to migrate to an oil-service contract or make some other change to acknowledge that it is essentially a marginal producer. Moscoso noted contractual changes would be a time-consuming process but can be done, and the GOE will be holding meetings with City Oriente on the issue.

18. (SBU) Moscoso was unclear about what might happen with contract renegotiations with non-U.S. companies in the petroleum sector. He made no indication of how the contracts might change, saying only that the process still needed to be defined. He noted that contract renegotiation with petroleum companies will definitely take place, but stressed it will be a "negotiation" with the companies, implying that the GOE will not simply impose new requirements.

#### Possible Changes in the Mining Sector

19. (SBU) Moscoso stressed the need for a clear policy on mining and mentioned the possibility of a separate mining ministry to handle issues in the sector. He stated that the current mining law is a "disaster for the state" and favors mining companies inordinately. In addition, he believes the law does not impose strict enough environmental rules on mining operations. (Comment: Implicit in Moscoso's comments is that the GOE would seek reforms to the mining sector to greatly increase the state's share of mining revenue and to tighten environmental requirements.)

Comment:

10. (SBU) Paralleling the tone of Energy Minister Acosta (Ref c), Moscoso appeared to be relatively practical about addressing problems in the energy sector, noting the importance of foreign investment and of working with U.S. firms to solve outstanding investment disputes. The decision to participate in the Oxy arbitration is a welcome indication that the government will work with established international procedures and is willing to make correct but politically difficult decisions. In addition, his comments regarding contract renegotiation with petroleum companies suggest the GOE might approach this in an even-handed manner that will take the concerns of both sides into account. Moscoso appears to recognize the importance of foreign investment to the energy sector in Ecuador, and that to encourage this investment the GOE must abide by its international legal obligations and work

cooperatively with foreign investors. An old government hand (he was previously a Petroecuador attorney), he commented wryly that many new administration members are from academia and had espoused impractical policies, but that "they are learning." Moscoso's practical approach and government experience may be a positive influence in the Energy Ministry, but it remains to be seen if his comments will translate into positive actions.

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